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SUBJECT: DONORS AND FRIENDS: THE WAY AHEAD

¶1. (SBU) Summary. Given Pakistan's struggling economy and the urgent need for development and budgetary assistance, Mission recommends that we move forward as quickly as possible to facilitate a successful Donors' Conference, co-hosted by the World Bank, and now tentatively scheduled for April in Tokyo. The "Friends of Democratic Pakistan" is floundering within the GOP, there is significant confusion about how to differentiate Friends and Donors, and it now appears that many countries would prefer to provide project rather than budgetary support at the Donors' Conference.

¶2. (SBU) Rather than split the limited resources of the donor community, therefore, we recommend that: (1) the Friends and the Donors be combined into one group; (2) Washington approach Friends' capitals to seek their agreement to this merger; and (3) USAID, through its Competitiveness Support Fund, immediately provide the GOP with a much-needed consultant to prepare for Tokyo. Based on informal consultations with Friends' embassies in Islamabad and Jean Arnault, the unannounced UN Friends Advisor, we believe that all parties will support efforts to merge these two initiatives and give Arnault a larger role in coordinating donor support. The majority of players continues also to support establishment of a Border Trust Fund. End Summary

Quick Injection of Funds Needed

¶3. (SBU) The GOP has been making heroic efforts to meet the conditions of its Standby Arrangement with the IMF. The IMF resident representative has noted that the IMF program is well underway. However, the fiscal tightening is causing a significant slowdown in the economy. Large scale manufacturing, for example, has declined by 5.6 percent in the first five months of the fiscal year (which ends June 30). GOP support for development projects, such as U.S.-Pakistan scholarship programs, is being cut off. It would be helpful if a donors' conference took place quickly in order to nail down the additional \$4 billion the IMF has estimated that the GOP will need to keep budgetary stringency from having serious repercussions. The IMF would prefer that this assistance take the form of direct budgetary support, something that many donors are reluctant to do, preferring to fund specific projects.

"Friends" is Floundering

¶4. (SBU) The Friends initiative is floundering within the GOP, which

has repeatedly postponed the proposed experts' meetings -now tentatively scheduled for mid-March. The MFA has tentatively agreed to move forward to invite seven additional countries - the Nordics, Malaysia, South Korean, and Russia (unless the U.S. objects) but has not issued any invitations. They have yet to make a formal announcement of Jean Arnault's appointment as UN Advisor to the Friends.

¶15. (SBU) Although Salman Farouqi, the General Secretary for the Presidency, reportedly has taken overall control of the initiative, he continues to delegate coordination to the MFA, which lacks the power to deliver. The MFA has suggested that Pakistan would welcome some much needed assistance in shaping its donor proposals.

¶16. (SBU) To date, we are not aware that Pakistan has formally approached the World Bank about creating and managing a Border Trust Fund, and there continues to be discussion about the geographic scope of this Fund's activities. Friends' embassies continue to support the concept in general, but they also would like clarity on its scope.

Merge Friends and Donors

¶17. (SBU) In trying to write project proposals, the GOP continues to struggle with what differentiates Friends from Donors. At a meeting of Friends' members January 30 at the Embassy, there was also a discussion of the difficulty in distinguishing among Friends and "others" at a Donors' Conference, with other donors perhaps feeling less integral to the process.

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¶18. (SBU) Post understands from discussions with local World Bank representatives and other potential donors that many countries will be reluctant to provide the GOP with direct budgetary support at the Donors' Conference and, instead, will be looking for projects to fund. Thus, the distinction between the two initiatives is becoming even more blurred.

Longer-Term Donor Coordination

¶19. (SBU) Beyond the Donors' Conference, Post has found strong support among Friends' embassies for proposed UN Advisor Jean Arnault's suggestion that he focus on broader donor coordination around an integrated development/security policy focus. Recognizing that donor support will come through a variety of bilateral and multilateral fora, Arnault agrees on the utility of a Trust Fund.

Help Needed

¶10. (SBU) To respond to the GOP's urgent need for assistance in shaping its proposals for the donor community, USAID proposes that it immediately hire, through its Competitiveness Support Fund, one of several senior ex-World Bank Pakistani experts who are already in country. Secondly, we can encourage the GOP to work more closely with the World Bank in its traditional role of macroeconomic coordination of donor assistance. The visiting regional Managing Director recently expressed the Bank's interest in doing more to assist the GOP in this regard.

Recommendations

¶11. (SBU) Post recommends: (1) we combine the two initiatives and keep Jean Arnault as UN Advisor working via UNDP to coordinate donor contributions; (2) Washington approach Friends' capitals to seek their agreement for this proposed change; and (3) that USAID immediately identify and fund a consultant to help the GOP prepare for Tokyo, working through the Ministry of Finance and the Competitiveness Support Fund.

PATTERSON